

Appendix L

RWSP Financial Policies



## RWSP Financial Policies

A. Under the provisions of the King County Charter and RCW 35.58.200, these financial policies are hereby adopted and declared to be the principal financial policies of the comprehensive water pollution abatement plan for King County, adopted by the Municipality of Metropolitan Seattle (Metro) in Resolution No. 23, as amended, and the RWSP, a supplement to the plan.

### B. Explanatory material.

1. Financial forecast and budget. Policies FP-1 through FP-7\* are intended to guide the county in the areas of prudent financial forecasting and budget planning and are included to ensure the financial security and bonding capacity for the wastewater system. This set of policies also addresses the county's legal and contractual commitments regarding the use of sewer revenues to pay for sewer expenses.

2. Debt financing and borrowing. Policies FP-8\* through FP-11\* are intended to guide the county in financing the wastewater system capital program. These policies direct that capital costs be spread over time to keep rates more stable for ratepayers by the county issuing bonds. A smaller share of annual capital costs will be funded directly from sewer rates and sewer revenues and capacity charges.

3. Collecting revenue. Policies FP-12\* through FP-14\* are intended to guide King County in establishing annual sewer rates and approving wastewater system capital improvement and operating budgets. Monthly sewer rates, which are the primary source of revenue for the county's regional wastewater system, are to be uniformly assessed on all customers. Customers with new connections to the wastewater system will pay an additional capacity charge. The amount of that charge is set by the council, within the constraints of state law.

4. Community treatment systems. Policy FP-15\* is intended to guide the county in the financial management of community treatment systems.

\*King County Code Reviser's note: Ordinance 15602 added new policies FP-3, FP-4 and FP-5, but this reference was not changed.

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FP-1: The county shall maintain for the wastewater system a multiyear financial forecast and cash-flow projection of six years or more, estimating service growth, operating expenses, capital needs, reserves and debt service. The financial forecast shall be submitted by the executive with the annual sewer rate ordinance.	A six-year financial plan is submitted each year with the WTD sewer rate proposal and, again, with the annual budget proposal.
FP-2: If the operations component of the proposed annual wastewater system budget increases by more than the reasonable cost of the addition of new facilities, increased flows, new programs authorized by the council, and inflation, or if revenues decline below the financial forecast estimate, a feasible alternative spending plan shall be presented, at the next quarterly budget report, to the council by the executive identifying steps to reduce	There were no occurrences of the situation described in FP-2 in 2004–2006, nor are any anticipated for the near-term. If such a situation were to occur, this policy would be implemented.

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cost increases. <i>(Ordinance 15602 amended this policy by splitting the policy into two policies, FP-2 and FP-3.)</i>	
FP-3: The executive shall maintain an ongoing program of reviewing business practices and potential cost-effective technologies and strategies for savings and efficiencies; the results shall be reported in the annual budget submittal and in an annual report to the RWQC. <i>(This policy was previously included as part of FP-2; Ordinance 15602 made this into its own policy.)</i>	The WTD Productivity Initiative is an ongoing systematic and comprehensive program for identifying ways to increase efficiency. This ten-year incentive program applies certain private-sector business practices, including an incentive-based cash payment to employees in the wastewater program, to cut operating costs, increase productivity and continue a high level of service and environmental protection for WTD's customers. A productivity report is submitted annually to the King County Council. Through 2006, the Productivity Initiative Pilot Program has resulted in a \$42.8 million savings to ratepayers.  Summary information from this report for 2006 is included in Chapter 13 of this report. Summary information from future reports will be included in future RWSP annual reports.
FP-4: New technologies or changes in practice that differ significantly from existing technologies or practices shall be reported to the council and RWQC with projected costs prior to implementation and shall also be summarized in the RWSP annual report. <i>(Ordinance 15602 added this policy to the RWSP financial policies.)</i>	No new technologies or changes in practice that differ significantly from existing technologies or practices are under consideration for implementation.
FP-5: Significant new capital and operational initiatives proposed by the Executive that are not within the scope of the current RWSP nor included in the RWSP, or are required by new state or federal regulations will be reviewed by the RWQC and approved by the council to ensure due diligence review of potential impacts to major capital projects' schedules, including Brightwater, the bond rating or the sewer rate and capacity charge. <i>(Ordinance 15602 added this policy to the RWSP financial policies.)</i>	All capital and operational costs are reviewed as part of the annual budget adoption process. No initiatives of this type were included in either the capital or operating budget requests in 2004–2006.
FP-6: The county shall maintain for the wastewater system a prudent minimum cash balance for reserves, including but not limited to, cash flow and potential future liabilities. The cash balance shall be approved by the council in the annual sewer rate ordinance.	Cash balance reserves are reviewed as part of the annual sewer rate and budget adoption process. In addition, cash reserve balances are reviewed annually with the bond rating agencies.
FP-7: Unless otherwise directed by the council by motion, the King County department of natural resources and parks or its successor agency shall charge a fee that recovers all	All work performed by WTD for other public or private organizations has required the recovery of all direct and indirect costs.

Financial Policies	How Implemented in 2004–2006
<p>direct and indirect costs for any services related to the wastewater system provided to other public or private organizations.</p>	<p>The one and one-half percent of annual operating budget limit on “Culver” funds is strictly adhered to.</p> <p>This policy was amended by Ordinance 15602 based on concerns raised by MWPAAC and Suburban Cities Association members on the Regional Water Quality Committee. They requested that the county investigate alternative funding sources for water quality improvement activities.</p> <p>In April 2007, The King County Executive submitted to the King County Council a report on alternative methods to provide a similar level of funding assistance for water quality improvement activities. More details on this report are provided in Chapter 13 of this report.</p>
<p>FP-8: Water quality improvement activities, programs and projects, in addition to those that are functions of sewage treatment, may be eligible for funding assistance from sewer rate revenues after consideration of criteria and limitations suggested by the metropolitan water pollution abatement advisory committee, and, if deemed eligible, shall be limited to one and one half percent of the annual wastewater system operating budget. An annual report on activities, programs and projects funded will be made to the RWQC. Alternative methods of providing a similar level of funding assistance for water quality improvement activities shall be transmitted to the RWQC and the council within seven months of policy adoption.</p> <p><i>(Ordinance 15602 amended this policy; it replaced the last sentence, which previously stated: “This policy shall remain in effect until such time as a financial plan for the surface water regional needs assessment is adopted and implemented.” with “Alternative methods of providing a similar level of funding assistance for water quality improvement activities shall be transmitted to the RWQC and the council within seven months of policy adoption.”)</i></p>	
<p>FP-9: The calculation of general government overhead to be charged to the wastewater system shall be based on a methodology that provides for the equitable distribution of overhead costs throughout county government. Estimated overhead charges shall be calculated in a fair and consistent manner, utilizing a methodology that best matches the estimated cost of the services provided to the actual overhead charge. The overall allocation formula and any subsequent modifications will be reported to the RWQC.</p>	<p>Overhead costs of King County general government are allocated by the Executive budget office to all parts of the county on a consistent basis.</p>
<p>FP-10: The assets of the wastewater system are pledged to be used for the exclusive benefit of the wastewater system including operating expenses, debt service payments, asset assignment and the capital program associated therewith. The system shall be fully reimbursed for the value associated with any use or transfer of such assets for other county government purposes. The executive shall provide reports to the RWQC pertaining to any</p>	<p>There have been no transfers of assets in 2004–2006.</p>

<b>Financial Policies</b>	<b>How Implemented in 2004–2006</b>
significant transfers of assets for other county government purposes in advance of and subsequent to any such transfers.	
FP-11: The county shall structure bond covenants to ensure a prudent budget standard.	Bond covenants are strictly followed, monitored, and revised to maintain prudent and conservative standards. Outstanding bonds are constantly monitored for refunding opportunities to lower interest rates/debt service. In 2004 and 2006 \$62 million and \$171 million in bonds were refunded respectively.
FP-12: King County should structure the term of its borrowings to match the expected useful life of the assets to be funded.	In 2007, WTD increased the term of bonds issued to 40 years. In addition to moderating the impact to current sewer rates, this provides a better match between the life of the facilities and the debt financing their construction.
FP-13: The wastewater system's capital program shall be financed predominantly by annual staged issues of long-term general obligation or sewer revenue bonds, provided that: All available sources of grants are utilized to offset targeted program costs; Funds available after operations and reserves are provided for shall be used for the capital program; excess funds accumulated in reserves may also be used for capital; Consideration is given to competing demands for use of the county's overall general obligation debt capacity; and Consideration is given to the overall level of debt financing that can be sustained over the long term given the size of the future capital programs, potential impacts on credit ratings, and other relevant factors such as intergenerational rate equity and the types of projects appropriately financed with long-term debt.	WTD capital expenditures are predominantly funded by the issuance of Sewer Revenue Bonds. County General Obligation Bonds are not expected to be a significant portion of new debt issuance. Through 2004, funds from meeting debt-service coverage requirements were transferred to the capital program. Beginning in 2005, funds from meeting debt-service coverage requirements are transferred to the capital program and the rate stabilization fund.
FP-14: To achieve a better maturity matching of assets and liabilities, thereby reducing interest rate risk, short-term borrowing shall be used to fund a portion of the capital program, provided that: Outstanding short-term debt comprises no more than fifteen percent of total outstanding revenue bonds and general obligation bonds; and Appropriate liquidity is available to protect the day-to-day operations of the system.	Short-term (junior lien) debt is targeted for approximately 15 percent of the total debt issued. Year-end liquidity reserves are targeted at 15 percent of the year's operating expense total.
FP-15: King County shall charge its customers sewer rates and capacity charges sufficient to	Beginning in 2002, WTD was reorganized to include an asset management section to reinforce the emphasis and visibility on maintaining the current assets of the

Financial Policies	How Implemented in 2004–2006
<p>cover the costs of constructing and operating its wastewater system. Revenues shall be sufficient to maintain capital assets in sound working condition, providing for maintenance and rehabilitation of facilities so that total system costs are minimized while continuing to provide reliable, high quality service and maintaining high water quality standards.</p>	<p>utility.</p>
<p>1. Existing and new sewer customers shall each contribute to the cost of the wastewater system as follows:</p>	<p>King County maintains a uniform monthly sewer rate in accordance with this policy.</p>
<p>a. Existing customers shall pay through the monthly sewer rate for the portion of the existing and expanded conveyance and treatment system that serves existing customers.</p>	<p>The sewer rate is set on an annual basis such that, given projections of other revenues and costs, the revenue requirements for providing wastewater services are met.</p>
<p>b. New customers shall pay costs associated with the portion of the existing wastewater conveyance and treatment system that serves new customers and costs associated with expanding the system to serve new customers. New customers shall pay these costs through a combination of the monthly sewer rate and the capacity charge. Such rates and charges shall be designated to have growth pay for growth.</p>	<p>The recent refinancing of certain bond series has lifted bond covenants that constrained the creation of a true rate stabilization reserve. Under the old parity bond covenants, revenues earned in one year could be recognized only in that year, forcing all excess operating revenues to be used to fund capital projects. This reduced the utility's borrowing needs; however, the resulting reduction in debt service had only a modest impact on the subsequent year's rate. With a rate stabilization reserve, excess revenues generated in the first year of a multi-year rate can be treated as operating revenues for the subsequent year. These revenues therefore can be applied directly to debt coverage requirements in the subsequent year, allowing for a reduction of the multi-year rate. For example, the adopted 2007 rate includes the use of such a reserve with a year-end 2007 reserve balance projected to be \$20 million. The full amount of this reserve is projected to be used in 2008 to keep the sewer rate level. The use and planned use of the rate stabilization funds are included in the rate transmittal. Information on the rate stabilization account is included in the annual sewer rate briefing to RWQC.</p>
<p>2. Sewer rate. King County shall maintain a uniform monthly sewer rate expressed as charges per residential customer equivalent for all customers.</p>	<p>The debt service coverage minimum is based on meeting two ratios, 1.25 on parity debt and a target of 1.15 on all debt.</p>
<p>a. Sewer rates shall be designed to generate revenue sufficient to cover, at a minimum, all costs of system operation and maintenance and all capital costs incurred to serve existing customers.</p>	<p>The capacity charge is based on the methodology listed in this policy.</p>
<p>b. King County should attempt to adopt a multiyear sewer rate to provide stable costs to sewer customers. If a multiyear rate is established and when permitted upon the retirement by the county of certain outstanding sewer revenue bonds, a rate stabilization reserve account shall be created to ensure that adequate funds are available to sustain the rate through completion of the rate cycle. An annual report on the use of funds from this rate stabilization account shall be provided annually to the RWQC.</p>	
<p>c. The executive, in consultation with the RWQC, shall propose for council adoption policies to ensure that adequate debt service coverage and emergency reserves are</p>	

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established and periodically reviewed.

3. Capacity charge. The amount of the capacity charge shall be a uniform charge, shall be approved annually and shall not exceed the cost of capital facilities necessary to serve new customers. The methodology that shall be applied to set the capacity charge is set forth in FP-12.3.a\*.

a. The capacity charge shall be based on allocating the total cost of the wastewater system (net of grants and other non rate revenues) to existing and new customers as prescribed in this subsection. The total system cost includes the costs to operate, maintain, and expand the wastewater system over the life of the RWSP. Total estimated revenues from the uniform monthly rate from all customers and capacity charge payments from new customers, together with estimated non rate revenues, shall equal the estimated total system costs. The capacity charge calculation is represented as follows:

$$\text{Capacity Charge} = \frac{[\text{Total system costs} - \text{rate revenue from existing customers}] - \text{Rate revenue from new customers}}{\text{Number of new customers}}$$

where:

(1) total system costs (net of grants and other non rate revenues) minus rate revenue from existing customers equals costs allocated to new customers.

(2) costs allocated to new customers minus rate revenue from new customers equals the total revenue to be recovered through the capacity charge.

(3) total capacity charge revenue requirements divided by the total number of new customers equals the amount of the capacity charge to be paid by each new customer.

b. The capacity charge may be paid by new customers in a single payment or as a monthly charge at the rate established by the council. The county shall establish a monthly capacity charge by dividing that amount by one hundred eighty (twelve monthly payments per year for fifteen years). The executive shall transmit for council adoption an ordinance to adjust the discount rate for lump sum payment. The executive shall also transmit for council

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Financial Policies	How Implemented in 2004–2006
<p>adoption an ordinance to adjust the monthly capacity charge to reflect the county's average cost of money if the capacity charge is paid over time.</p>	
<p>c. King County shall pursue changes in state law to enable the county to require payment of the capacity charge in a single payment.</p>	
<p>d. The capacity charge shall be set such that each new customer shall pay an equal share of the costs of facilities allocated to new customers, regardless of what year the customer connects to the system. The capacity charge shall be based upon the costs, customer growth and related financial assumptions used for the Regional Wastewater Services Plan adopted by Ordinance 13680 as such assumptions may be updated. Customer growth and projected costs, including inflation, shall be updated every three years beginning in 2003.</p>	
<p>e. The county should periodically review the capacity charge to ensure that the actual costs of system expansion to serve new customers are reflected in the charge. All reasonable steps should be taken to coordinate the imposition, collection of and accounting for rates and charges with component agencies to reduce redundant program overhead costs.</p>	
<p>f. Existing customers shall pay the monthly capacity charge established at the time they connected to the system as currently enacted by K.C.C. 28.84.055. New customers shall pay the capacity charge established at the time they connect to the system.</p>	
<p>g. To ensure that the capacity charge will not exceed the costs of facilities needed to serve new customers, costs assigned and allocated to new customers shall be at a minimum ninety five percent of the projected capital costs of new and existing treatment, conveyance and biosolids capacity needed to serve new customers.</p>	
<p>h. Costs assigned and allocated to existing customers shall include the capital cost of existing and future treatment, conveyance and biosolids capacity used by existing customers, and the capital costs of assessing and reducing infiltration and inflow related to the use of the existing conveyance and treatment capacity.</p>	
<p>i. Capital costs of combined sewer</p>	

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overflow control shall be paid by existing and new customers based on their average proportionate share of total customers over the life of the RWSP.

j. Operations and maintenance costs shall be paid by existing and new customers in the uniform monthly rate based on their annual proportionate share of total customers.

k. Any costs not allocated in FP-12.3 f, g, h, i and j\* shall be paid by existing and new customers in the sewer rate.

l. Upon implementation of these explicit policies, the Seattle combined sewer overflow benefit charge shall be discontinued.

4. Based on an analysis of residential water consumption, as of December 13, 1999, King County uses a factor of seven hundred fifty cubic feet per month to convert water consumption of volume-based customers to residential customer equivalents for billing purposes. King County shall periodically review the appropriateness of this factor to ensure that all accounts pay their fair share of the cost of the wastewater system.

\*King County Code Reviser's note: Ordinance 15602 added new policies FP-3, FP-4 and FP-5, but this reference was not changed.

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FP-16: The executive shall prepare and submit to the council a report in support of the proposed monthly sewer rates for the next year, including the following information:

Key assumptions: key financial assumptions such as inflation, bond interest rates, investment income, size and timing of bond issues, and the considerations underlying the projection of future growth in residential customer equivalents;

Significant financial projections: all key projections, including the annual projection of operating and capital costs, debt service coverage, cash balances, revenue requirements, revenue projections and a discussion of significant factors that impact the degree of uncertainty associated with the projections;

Historical data: a discussion of the accuracy of the projections of costs and revenues from previous recent budgets, and

Policy options: calculations or analyses, or both, of the effect of certain policy options on the overall revenue requirement.

These options should include alternative capital

All key assumptions, significant financial projections, historical results, and policy options are provided as part of the annual sewer rate submittal letter and attachments.

<b>Financial Policies</b>	<b>How Implemented in 2004–2006</b>
program accomplishment percentages (including a ninety percent, a ninety-five percent and a one hundred percent accomplishment rate), and the rate shall be selected that most accurately matches historical performance in accomplishing the capital program and that shall not negatively impair the bond rating.	
FP-18: The cost of community treatment systems developed and operated in accordance with WWSP-15 would not be subsidized by the remaining ratepayers of the county's wastewater treatment system.	This policy has been adhered to since the adoption of the RWSP.